78-1781

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

In the Matter

—of—

JACOB P. LEFKOWITZ,

Bankrupt-Petitioner.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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To:

THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Petitioner prays that a writ of certiorari issue to review the judgment herein of the United States Court of Appeals for the Second Circuit (Timbers, C.J., Meskill, C.J., and Owen, D.J., sitting by designation) entered in the above-entitled case on March 2, 1979, affirming an order and opinion of the District Court for the Southern District of New York (Pierce, D.J.) dated June 30, 1978 and September 5, 1978, respectively, which affirmed the decision of the Honorable Howard Schwartzberg, Bankruptcy Judge dated September 28, 1976, denying the bankrupt his discharge.

Citations to Opinions Below

The decision of the Bankruptcy Court is reported in 10 C.B.C. 570, and is printed, *infra*, App. D, 12a-26a.* The opinion of the District Court is unreported and is printed, *infra*, App. B, 4a-10a.

The opinion of the Court of Appeals for the Second Circuit is reported at —— F.2d —— and is printed, *infra*, App. A, 1a-3a.

Jurisdiction

The judgment of the Court of Appeals for the Second Circuit was made and entered on March 2, 1979. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

Questions Presented

1. Does the Bankruptcy Act and Rules require the bankrupt to first prove the adequacy of his financial records where admittedly no records were destroyed or concealed and the bankrupt produced *all primary or original records*, such as, checkbooks, deposit slips, bank statements, cancelled checks, and the like, *before* a party objecting to his discharge need demonstrate the facts essential to the objection?

2a. Whether the Court below erred, by misconstruing and misapplying Section 14(c) of the Bankruptcy Act, 11 U.S.C., Section 32(c) 1976, and Congress' intent by imposing an unduly harsh standard as to the adequacy of

* References to "a" are to pages in the appendix to this petition, *infra*.

the bankrupt's books and records merely because of his profession, unjustly denying the bankrupt his discharge?

b. Considering the rehabilitative intent of the Bankruptcy Act, did the Court below err in failing to remand, to permit the bankrupt to organize, i.e., write up in ledgers his primary or original records so that these secondary ledgers or records would then reflect his financial condition and business transactions?

Statutes Involved

The statutory provisions specifically involved are 14(c) of the Bankruptcy Act, 11 U.S.C. Section 32(c) (1976) and Rule 407 of the Rules of Bankruptcy Procedure. The specific provisions cited are reproduced, *infra*, App. E, 27a.

Statement of the Case

On January 27, 1975, Jacob P. Lefkowitz, (the bankrupt) filed a voluntary petition in bankruptcy in the United States District Court for the Southern District of New York, and was duly adjudicated as such.

In an undated complaint annexed to a summons and notice of trial issued on November 10, 1975, pursuant to Section 14 of the Bankruptcy Act, 11 U.S.C. Section 32, the trustee in bankruptcy commenced an adversary proceeding before the Bankruptcy Court to deny the bankrupt his discharge. The trustee alleged three separate charges: 1) the bankrupt failed to keep books of account or records from which his financial condition and business transactions might be ascertained, within meaning of Section 14c(2) of the Bankruptcy Act; 2) the bankrupt committed an offense punishable by imprisonment as provided under

Title 18, United States Code, Section 152, as set forth in Section 14c(1) of the Bankruptcy Act, in that he knowingly and fraudulently made a false oath; and 3) the bankrupt failed to explain satisfactorily losses in assets to meet his liabilities.

At the outset of the trial, the trustee withdrew the third charge and the Bankruptcy Judge subsequently dismissed the second charge as a result of failure of proof. Remaining then was the charge that the bankrupt failed to keep or preserve books of account from which his financial condition and business transactions might be ascertained as mandated by Section 14(c) of the Bankruptcy Act.

The debts of the bankrupt arose between 1962 and 1974. During this period, the bankrupt was and still is a practicing attorney specializing in criminal law. He was engaged in no other business or occupation. The bankrupt, in a moment of lapse, had incurred a heavy gambling loss and in 1964, started borrowing large sums of money to satisfy same. Although the bankrupt's present gross receipts were substantial, considering he handled only 10-20 clients per year, he suffered severe financial difficulty caused by the original gambling plight, his borrowing to cover same, and his subsequent efforts to repay these loans and their usurious interest.

Although the bankrupt did not maintain secondary records, such as cash disbursement ledgers, purchases ledgers, and the like, the bankrupt did keep and maintain *extensive original records,* in the same manner as he always did for the past 40 years as a practicing attorney. These consisted of *all original records,* such as, checkbooks, diaries, cancelled checks, bank statements, deposit slips, a pocket memorandum recording his short term loans, 11 sheets of memoranda referring to his long term loans, a vast amount of promissory notes and letters from lenders.

As a result of the commencement of numerous law suits, the bankrupt filed his voluntary petition in bankruptcy. He turned over to the trustee *all of his original records* as above set forth, from the years 1970 through 1974, including his income tax returns.

No dispute has ever been raised that they were not complete and intact, i.e., each monthly bank statement was correlated with related deposit slips and cancelled checks, etc. At the hearing on discharge, these records which had been in possession of the trustee for many months, did not appear in the manner they had been received. The trustee disrupted the entire correlation of the bankrupt's records by removing the original checks and deposit slips for an entire year and placing each in separate bundles or categories, with utter disregard as to their original chronological order, thereby completely disrupting the bankrupt's system of correlation and record keeping.

Notwithstanding the fact that he, the trustee, had complete records back to the year 1970, he proceeded to examine the bankrupt, at random, concerning the years 1973 and 1974 only, using selected bits and pieces of the original records. Nevertheless, at no time did the bankrupt fail, nor was he ever at a loss, to satisfactorily answer and explain, all questions concerning the random records selected, despite the trustee's tampering with their continuity and disrupting their original orderly correlation.

From the records maintained by the bankrupt, it is manifestly clear that he kept and preserved books and records from which his financial condition and business transactions could be ascertained.

The uncontradicted testimony of both the bankrupt and the accountant for the bankrupt was never rebutted by the trustee. The bankrupt kept voluminous records which he

turned over to the trustee for the years 1970 through 1974. His fees were accounted for, his borrowing activities and repayments of interest and principal were explained in great detail. All lenders were listed as creditors on the schedules. Numerous notes and memoranda were produced, which, together with his testimony, substantiated payments of principal and interest, to the effect that when all the bankrupt's records, diaries, deposit slips, checkbooks, cancelled checks, memoranda, etc. were correlated, his financial affairs were made clear. His unrebutted testimony, the veracity and accurateness of which was never in issue nor questioned, left no confusion or nothing to the imagination. The credibility of the bankrupt is unquestionably admitted by the record.

In spite of the completeness of the bankrupt's records, and his ability to answer *in toto* all questions propounded to him, the Bankruptcy Judge denied the bankrupt his discharge and the District Court and Court of Appeals affirmed.

In essence, the bankrupt has been denied his discharge because he did not write up in a secondary ledger his receipts and disbursements, notwithstanding that he produced and turned over *all of his primary or original books and records.*

Reasons For Granting the Writ

1. The Court of Appeals' decision affirms a construction and interpretation of Rule 407 of the Rules of Bankruptcy Procedure, which is in total disregard of the manifest Congressional intent, embodied in the Bankruptcy Act and Rules. If this decision is allowed to stand, the intent will be seriously undermined.

It is a well accepted fundamental principal that the intent of the Bankruptcy Act and Rules is to give the honest debtor the opportunity to financially rehabilitate himself so as to get a fresh start in life free from debt. *In Re Kokoszka,* 479 F.2d 990, 997 (CA-2, 1973), *aff'd. sub nom., Kokoszka* v. *Belford,* 417 U.S. 642 (1974), *Local Loan Co.* v. *Hunt,* 292 U.S. 234 (1933). As most voluntary straight bankruptcy proceedings are filed for the purpose of receiving a discharge and a denial of discharge is the loss of the principal benefit of bankruptcy to the bankrupt, those statutory provisions relating to discharge, Section 14(c), have been construed in a restrictive fashion wherever possible. *Local Loan Co.* v. *Hunt, supra, International Shoe Co.* v. *Lewine,* 68 F.2d 517, 518 (CA-5, 1934), *Gross* v. *Fidelity & Deposit Co.,* 302 F.2d 338, 341 (CA-8, 1962).

These rules of construction are consistent with the fact that although Bankruptcy Courts are vested with jurisdiction of law under the Bankruptcy Act, they are essentially Courts of equity and their proceedings are inherently proceedings in equity. Thus, Courts of Bankruptcy must employ due consideration as to the remedial nature of the Act, as well as to general equitable principles in their decisions concerning a bankrupt. *Katchen* v. *Landy,* 382 U.S. 323 (1966), *Marin* v. *England,* 385 U.S. 99 (1966), *Pepper* v. *Litton,* 308 U.S. 295 (1939), *Local Loan Co.* v. *Hunt, supra.*

Rule 407 of the Bankruptcy Rules, effective October 1, 1973, provides that:

> "At a trial on a complaint objecting to discharge, the plaintiff has the burden of proving the facts essential to this objection."

This Rule, patterned after Section 500 of the California Evidence Code, supercedes and alters the proviso at the

end of Section 14(c). This proviso, formulated in 1926 and retained under the Act of 1938, provided that:

> "If upon the hearing of an objection to discharge, the objector shall show, to the satisfaction of the Court, that there are reasonable grounds for believing that the bankrupt has committed any one of the acts which . . . prevent discharge in bankruptcy, then the burden of proving that he has not committed any such act shall be upon the bankrupt."

A cursory reading shows the drastic difference between the burdens imposed upon the bankrupt during an adversary proceeding objecting to his discharge. Under 14(c), if an objector had made reasonable showing that the bankrupt had committed acts capable of blocking his discharge, then the burden shifted to him to disprove that those acts were not committed. Thus, once an objector had shown reasonable grounds for the Court to believe that the bankrupt failed to keep books and records, the burden shifted to the bankrupt to explain why he did not keep them, or if he did have them, account for their incompleteness or for their disappearance. 1a *Collier on Bankruptcy*, 14 Ed., Section 14.33 at 1371. In a state of equilibrium, the discharge could be denied. *In re Barbaire*, 97 F.Supp. 86 (E.D. Pa. 1951), *aff'd*. 192 F.2d 1018 (CA-3, 1951). Section 14(c) has been equated with requirement that the objector make a *prima facie* case. *In re Pioch*, 235 F.2d 903 (CA-3, 1956).

In contrast, the Bankruptcy Rule deals only with the burden of proof to be established by the objector that is, all the facts essential to his objection. Burden of proof means the obligation of a party to produce a particular state of conviction in the mind of the trier of fact as to the existence or nonexistence of a fact. Comment of California Law Revision Committee, Section 500 of the Evidence Code.

When a party seeks relief, the burden is on him to prove his case. Under Rule 407, the objector cannot depend wholly upon the failure of the bankrupt to prove his defenses.

The Rule does not directly deal with the bankrupt's burden of going forward with evidence, but the comment to the Rule states that:

> "Subject to the allocation of that rule of the initial burden of producing evidence and the alternate burden of persuasion the Rule leaves to the courts the formulation of rules governing the shift of the burden of going forward with the evidence in light of such considerations as the difficulties of proving the nonexistence of a fact and of establishing a fact into which the evidence is likely to be more accessible to the bankrupt than to the objector."

With the advent of Bankruptcy Rule 407, the emphasis, now, is upon the *objector* to prove his case, although that is subject to a duty on the party of the bankrupt to produce items more accessible to him, i.e., books and records. The objector must *"go beyond a showing of reasonable grounds and produce proof of facts which will establish that the bankrupt has committed the act charged before the burden of going forward with the evidence will shift to the bankrupt."* (Emphasis added) *1a Collier on Bankruptcy*, 14 Ed. Section 14.33 at 1373.

It is this distinction that the Courts below failed to discern. The Court of Appeals held:

> ". . . while Rule 407 places the burden of persuasion squarely on the objector, it leaves the burden of going forward for the Court to assign based on the particular circumstances, (Citations omitted) . . . therefore Rule 407 in no way relieves appellant of his burden of *producing adequate* records." (Emphasis added, 3a)

The District Court stated that:

> "With respect to the burdens to be imposed on the various parties, Rule 407 of the Rules of Bankruptcy Procedure provides that a plaintiff, here the trustee, has the burden of proving facts essential to his objection to the discharge. This rule does not change the *initial burden* which is placed upon the bankrupt of producing records from which his financial condition may be ascertained." (Emphasis added, 9a)

These statements show a total misunderstanding as to the intent of the Bankruptcy Act in general, and more specifically, Section 14(c) as affected by Rule 407. The trustee, under Section 14(c), had asserted that the bankrupt failed to produce records from which his financial condition and business transactions might be ascertained. The bankrupt's duty was to turn over all his records. His discharge would have been granted as a matter of course if the trustee had not affirmatively objected. *Liebke* v. *Thomas*, 116 U.S. 605 (1886). Thus, whatever records, if any, that were produced were adequate until proven otherwise, as Rule 407 clearly indicates. The burden to prove that they were *not adequate* rests with the objector.

To first require the bankrupt to *prove* that they are adequate, is a direct affront to the clear meaning of Rule 407 and contrary to the principal that controversies involving the discharge provisions of the Bankruptcy Act should be resolved in favor of the bankrupt. This fundamental premise continues to hold true for the new Bankruptcy Reform Act of 1978, Title 11 of the U.S. Code, which replaces the Bankruptcy Act of 1889 in its entirety. *Cong. Rec.*, Hon. Don. Edward (Rep.-Cal.), Jan. 4, 1977, E19, 21. The discharge provision, Section 727 the replacement of Section 14(c), remains the heart of the fresh start provisions of

the Bankruptcy Code. 11 U.S.C. Section 727, *Legislative History*. Sub. (a) of Section 727 requires the Court to grant a bankrupt a discharge unless one of the eight enumerated conditions of this section has been met (Section 727(a)(3) substantially retains 14(c)(2) of the old Act.) Thus, an objector must affirmatively prove that one of the conditions of this section has been met to block a discharge of the bankrupt. The standard of proof necessary is still contained in Rule 407.

Section 405(d) of the Bankruptcy Reform Act of 1978 states that the Bankruptcy Rules previously promulgated by this Court will remain effective to the extent that they are not inconsistent with the New Bankruptcy Code. Rule 407 remains intact, thus reevidencing Congress' intent that the bankrupt have every opportunity to relieve himself of his burdensome debt. Section 727, as with Section 14(c), read in conjunction with Rule 407, illustrates Congress' belief that a debtor wishing to take advantage of the Bankruptcy Code will be granted a discharge as a matter of law, unless and only if, a party comes forward and proves unilaterally that the bankrupt failed to meet one of the eight enumerated conditions under Section 727 or the old Section 14(c).

Certiorari should be granted so as to enable this Court to set a clear standard of proof required in objections to discharge under this section of the Bankruptcy Act and the New Bankruptcy Code.

2. The decision of the Court of Appeals sets an unduly harsh standard as to the adequacy of the bankrupt-petitioner's books and records because of his profession, denegrating the rehabilitory spirit of the Bankruptcy Act. Its harshness is in essential conflict with a similar situation involved in a decision of the Court of Appeals for the Fifth Circuit, *Goff* v. *Russel Company*, 495 F.2d 199 (CA-5, 1974).

It is an abberation of the spirit of the Bankruptcy Act to withhold the discharge of the bankrupt because he, as attorney, had not maintained an intricate accounting system. The Court of Appeals *In re Underhill*, 82 F.2d 258 (CA-2, 1936) cert. den. *Underhill* v. *Lent*, 299 U.S. 546 on the issue stated that:

> "the law is not unqualified in imposing a requirement to keep books and records, and it does not require that if they are kept, they shall be kept in any special form of accounts. It is a question in each instance of reasonableness in the particular circumstances. Complete disclosure is, in every case, a condition precedent to the granting of the discharge, and if such a disclosure is not possible without the keeping of books and records, then the absence of such amounts to that failure to which the Act applies."

In the instant case, there admittedly was no absence of books and records. The bankrupt completely disclosed his transactions via both memoranda, original records and unrebutted oral testimony. The bankrupt was penalized solely because of the lack of secondary accounting ledgers which are admittedly predicated upon original records and could have been written up by a qualified bookkeeper or accountant, if necessary.

Further, as stated in *White* v. *Schoenfeld*, 117 F.2d 131 (CA-2, 1941): "the bankrupt is generally required to produce such books and records as are customarily kept by persons doing the same kind of business, or to give adequate reasons why he was not bound to keep them."

"It is not the size of the enterprise alone which determines the necessity of keeping books, but also its nature."

Matter of Markham, 52 Am. Br. N.S. 366, 41 F.Supp. 94 (1941).

"What will justify that failure depends largely upon how extensive and complicated the bankrupt's business is. A cobbler will succeed with less than a manufacturer." *White* v. *Schoenfeld*, *supra*.

This bankrupt is a criminal attorney with 10 to 20 clients per year, a professional with very few transactions. The bankrupt was not unusual in the way he kept his affairs, i.e., out of a checkbook and deposit slips, etc. The accountant's testimony corroborated that the bankrupt's manner of keeping his financial affairs was the usual practice for single entrepreneurs.

The bankrupt's failure, *if any*, was to keep or maintain neatly written ledgers of receipts and disbursements. But it is obvious that the bankrupt, if required or given the opportunity, could have written up such a ledger because he had and maintained all of his original records, which is the source of such. Is the bankrupt to be penalized because he failed to have a bookkeeping department, when in fact, he had all original records from which such ledgers are synthesized?

In *Goff* v. *Russel Company*, 495 F.2d 199 (CA-5, 1974) the Fifth Circuit faced a similar situation but its decision reflected the spirit of the Act, which was to give the bankrupt every equitable opportunity possible to gain a discharge from burdensome debt. In this case, the bankrupt had operated several retail stores with a substantial amount of weekly gross receipts. Although he retained sales receipts and other records, they were not in good order. Evidence indicated that tax returns could not have been prepared nor could bank statements be reconciled with cash deposited and withdrawn. (Id. at 200)

The Fifth Circuit held that considering the complexity of all the facts and circumstances disclosed on the record, it was appropriate to remand the matter to the District Court with instructions to consider the possibility of allowing the bankrupt, at his own expense, to put his records in order.

Additionally, the Court of Appeals suggested that if the bankrupt's records then substantially "reflected his financial status", it could require the Bankruptcy Court to reconsider the denial of the bankrupt's discharge. (Id. at 202)

The bankrupt-petitioner produced *all* of his records for the years 1970 through 1974, inclusive of the time in question. His veracity was never questioned, neither was there any question of a failure to produce being motivated by a fraud of any kind. Consequently, the record clearly shows there was no prejudice to the objector or for that matter, to any creditor. Here in essence is where the Bankruptcy Judge's abuse of discretion lies, which was affirmed by the District and Circuit Courts. The bankrupt kept records. There was no denying that the objections to discharge was failure to keep and preserve records from which his financial condition prior to bankruptcy could be determined. This objection, however, hinged not only on the presence of the books and records, but also on the explanations of the bankrupt himself.

The Bankruptcy Court:

> "I think you put your finger right on the basic issue here. The basic issue is a disagreement, really, as to the interpretation of Section 14(c)(2); that is, *the trustee's position here is that the books and records must reveal the bankrupt's condition without any assistance from the bankrupt,* and the bankrupt's position is the books and records are satisfactory with

> (sic) supplemented—where the bankrupt explains the unity, and basically, that is the issue here." (Emphasis added)

It is clear the Bankruptcy Judge, with the concurrence of the District Court and the Court of Appeals, chose to follow the trustee's contention.

The Court of Appeals, because of the availability of all of the petitioner's original records, should have, as the Fifth Circuit did, remanded the matter to the District Court for further consideration.

Certiorari should be granted so as to make clear that the "primary purpose of the Bankruptcy Act is to enable a bankrupt, who is entitled to a discharge, to obtain such discharge promptly and to reestablish himself in business." *In re Fithina,* 156 F.Supp. 877, 879 (D.C. Md., 1957), and that every opportunity should be made to allow the bankrupt to avail himself of that entitlement to discharge.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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Appendices

APPENDIX A

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the 2nd day of March, one thousand nine hundred and seventy-nine.

Present:

HON. WILLIAM H. TIMBERS,
HON. THOMAS J. MESKILL,
Circuit Judges

HON. RICHARD OWEN,
United States District Judge
Sitting by Designation

78-5053

In the Matter

of

JACOB P. LEFKOWITZ,

Bankrupt-Appellant.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

Appendix A

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is *affirmed* on the opinion of Judge Pierce dated September 5, 1978.

Appellant, the bankrupt, appeals from an order of the district court which affirmed an order of the bankruptcy court denying the bankrupt a discharge because of the inadequacy of his financial records under § 14(c)(2) of the Bankruptcy Act, 11 U.S.C. § 32(c)(2)(1976).

Appellant contends, first, that the records he made available to the trustee were adequate to satisfy the record-keeping requirement of § 14(c)(2); and, second, that the district court improperly required him to disprove the trustee's objections to the adequacy of the records, rather than requiring the objector to prove his objection, as required by Bankruptcy Rule 407.

The law does not specify a uniform record-keeping standard. It requires only that the records kept shall be reasonable "in the particular circumstances." *In re Underhill*, 82 F. 2d 258, 260 (2 Cir.), *cert. denied*, 299 U.S. 546 (1936). Such circumstances include usual business practice in the field and the complexity of the enterprise, as well as the bankrupt's experience and education. *See, e.g., White* v. *Schoenfeld*, 117 F.2d 131 (2 Cir. 1941); *In re Underhill*, *supra*, 82 F.2d at 260. The large number of individuals to whom the instant bankrupt owed money—150—and the large amounts owed, most assuredly required the maintenance of careful records. Appellant's education and experience as an attorney should have put him on notice as to the importance of proper records. *See Hilliard* v. *Hollins*, 290 F.2d 263 (6 Cir. 1961) (lawyer had no record of collections from law practice, or of sale of $22,500 in timber rights, nor of some $100,000 in outstanding loans, but

Appendix A

had produced "a miscellany of bank deposit slips, check stubs, cancelled checks, and like material"; *held*, denial of discharge affirmed).

Moreover, the method proposed by appellant, even if it somehow had managed to present a picture of his financial condition and a record of his recent business transactions, still would have left the creditors with only his word as to how the bankrupt estate had been dissipated. This would have been at variance with the Act:

> "Records of substantial completeness and accuracy are required so that they may be checked against the mere oral statement of explanations made by the bankrupt. [citation omitted]" *In re Underhill, supra*, 82 F.2d at 260.

As for appellant's second contention, while Rule 407 places the burden of persuasion squarely on the objector, it leaves the burden of going forward for the court to assign based on the particular circumstances. *See* Advisory Committee Note to Rule 407; *In the Matter of Martin*, 554 F.2d 55, 58 (2 Cir. 1977), *cert. dismissed*, 434 U.S. 801 (1978). As the district court correctly held, therefore, Rule 407 in no way relieves appellant of his burden of producing adequate records.

Affirmed.

/s/ WILLIAM H. TIMBERS
William H. Timbers

/s/ THOMAS J. MESKILL
Thomas J. Meskill
Circuit Judges

/s/ RICHARD OWEN
Richard Owen
United States District Judge
Sitting by Designation

APPENDIX B

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN RE JACOB P. LEFKOWITZ,

Bankrupt.

APPEARANCES:

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LAWRENCE W. PIERCE, D.J.

OPINION

The bankrupt, Jacob P. Lefkowitz, appeals from an opinion and order of Howard Schwartzberg, Bankruptcy Judge, denying him discharge as provided by 11 U.S.C. §32 (1976) [§14 the Bankruptcy Act] on the grounds that the appellant-bankrupt failed to comply with §32(c) (2) of the Act which requires a bankrupt to maintain and to preserve books of accounts or records from which his financial condition and business transactions might be ascertained and that there was no justification for this failure.

Appendix B

The arguments raised on this appeal by the bankrupt attacking the bankruptcy judge's determination may be summarized as follows:

1. That the bankruptcy judge's findings of fact, numbers 5-17 and 19, are clearly erroneous.

2. That the bankruptcy judge erroneously placed the burden of proof with respect to the issue of the inadequacy of the bankrupt's records on the bankrupt.

3. That the bankruptcy judge abused his discretion in denying discharge.

The Court will address each argument in turn.

1. *Findings of Fact 5-17*

The evidence establishes that the bankrupt had been a practicing attorney specializing in criminal cases. While his practice consisted of only ten to twenty clients at any given time, his income for 1973 and 1974, the years in question, was $140,819 and $188,700, respectively. The bankrupt testified before the bankruptcy judge that the records reflecting his receipt of fees from clients during these two years were to be found by comparing his office diaries for these years with all his bank deposit slips, which he produced. He also testified that for the period between 1962 and 1974, he sustained heavy gambling debts, causing him to borrow sizeable amounts of money in order to purportedly repay the principal as well as the interest which at times ranged between 25% to 100%. With respect to this indebtedness and the repayment thereof, the bankrupt produced copies of cancelled checks; his income tax returns which allegedly indicate deductions for interest; copies of

"eleven pages of handwritten notes purporting to list the names of the bankrupt's long-term lenders, the dates the loans were made and the amount of interest to be paid to these lenders."; pages extracted from plaintiff's "pocket diary for the year 1974 reflecting his notations with respect to the names of individuals who loaned him money for short periods of time, together with the dates and interest to be paid"; a "bundle of handwritten sheets of paper containing signed receipts and notations of payment in 1974" (Tr. from Bankruptcy Court proceedings, p. 7, 8), and a number of promissory notes signed by the bankrupt which date back to 1970.

The bankruptcy judge reviewed each document produced by the bankrupt, as well as the testimony of the bankrupt himself and that of his accountant, in an effort to piece together the present financial condition of the bankrupt—findings of fact number 5-17. This effort proved unsuccessful. With respect to the bankrupt's income, the judge found that the deposit slips could not stand as evidence of the receipt of fees by the bankrupt since they contained no notation as to the source of the funds deposited. He made a similar finding with respect to the income tax returns since there was no independent documentation produced which supported the information contained therein. Regarding the loans, the judge found that neither the pages extracted from the bankrupt's pocket diary for 1974 nor the eleven pages purporting to list the names of the lenders could be used to ascertain the amount of money paid by the bankrupt toward these obligations and that the promissory notes did not establish the disposition of the funds which the bankrupt had on deposit.

Given the evidence before the bankruptcy judge and the lack of evidence, this Court cannot say that his findings

numbered 5-17 were clearly erroneous. See Rules Bankr. Proc. Rules 752 and 810.[1]

2. *Finding of Fact 19*

Finding of fact number 19 states:

"From the foregoing, it is evident that the disordered mass of documents produced by the bankrupt are inadequate to ascertain his financial condition and business transactions. The bankrupt has failed to sustain his burden of maintaining and presenting records in reasonably understandable form" [as provided by §14 (c)(2) of the Bankruptcy Act].

The bankrupt objects to this finding on two grounds: first, that it is contrary to the weight of the evidence presented

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[1] Rule 752 provides in pertinent part:

"(a) *Effect.* In all matters tried upon the facts without a jury or with an advisory jury, the court shall find the facts specially and state separately its conclusions of law thereon, and the judgment shall be entered pursuant to Rule 921(a). Requests for findings are not necessary for purposes of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses. If an opinion or memorandum of decision is filed, it will be sufficient if the findings of fact and conclusions of law appear therein. Findings of fact and conclusions of law are unnecessary on decisions of motions under these rules except when, on a motion to dismiss under Rule 741, the court renders a judgment on the merits after a trial on the facts."

Rule 810 provides in pertinent part:

"Upon an appeal the district court may affirm, modify, or reverse a referee's judgment or order, or remand with instructions for further proceedings. The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge of the credibility of the witnesses."

and, second, that the judge placed the burden of proof on the bankrupt in violation of Rule 407 of the Bankruptcy Act.[2]

The crux of the appellant's argument is that his testimony as to the details of the transactions allegedly reflected by the documents submitted to the bankruptcy court supplement the data contained in the documents received in evidence. The combination of testimonial and documentary evidence, appellant argues, adequately establishes his financial condition.

With respect to this argument, the Court notes that it is within the bankruptcy judge's discretion to determine the reasonableness of the method of record-keeping employed by the bankrupt. See *In re Halpern*, 387 F.2d 312, 315 (2d Cir. 1968); *In re Underhill*, 82 F.2d 258, 260 (2d Cir.), *cert. denied, sub nom. Underhill* v. *Lent*, 299 U.S. 546 (1936). (*A fortiori*, where the bankrupt is also an attorney, see *In re Manasse*, 125 F.2d 647, 649 (7th Cir. 1942)). Hence, the bankruptcy judge acted well within his authority in finding that an attorney *qua* bankrupt, who presents a myriad of documents which can be made intelligible only through his "interested" testimony—which the judge may or may not credit, has failed to adequately establish his financial condition as required by the Bankruptcy Act. See *Hedges* v.

[2] An issue exists as to whether a bankruptcy judge's determination made pursuant to §32(c)(2) is a question of fact, in which event the reviewing court must apply the "clearly erroneous" standard, see *Goff* v. *Russell*, 495 F.2d 199 (5th Cir. 1974); *White* v. *Schoenfeld*, 117 F.2d 131 (2d Cir. 1941); *In re Stein*, 416 F.Supp. 637 (E.D.N.Y. 1976) or whether such a determination is a conclusion of law, in which event a reviewing court has more latitude in reaching a different result than that of the bankruptcy judge. See *In re Sandow*, 151 F.2d 807 (2d Cir. 1945). Since the Court finds that under either standard of review the bankruptcy judge's findings were proper, the issue need not be definitively addressed.

Bushnell, 106 F.2d 979 (10th Cir. 1939). Accordingly, this Court finds appellant's argument which attacks the sufficiency of the evidence relied upon by the bankruptcy judge in making his findings to be without merit.

With respect to the burdens to be imposed on the various parties, Rule 407 of the Rules of Bankruptcy Procedure provides that a plaintiff, here the trustee, has the burden of proving facts essential to his objection to the discharge. This rule does not change the initial burden which is placed upon the bankrupt of producing records from which his financial condition may be ascertained. See Advisory Committee's Note to Bankruptcy Rule 407; *In re Martin*, 554 F.2d 55, 58 (2d Cir. 1977). This Court finds nothing in the record which indicates that the bankruptcy judge placed any burden on the bankrupt which is proscribed by Rule 407, and, thus, this argument by appellant is also without merit.

3. *Abuse of Discretion*

The bankruptcy judge, upon examination of the bankrupt's position and record, determined that the bankrupt should have maintained more detailed records. He concluded that the records produced did not meet the statutory mandate of being ". . . records, from which his financial condition and business transactions might be ascertained." §32(c)(2). Therefore, the bankruptcy judge justifiably based his decision on the bankrupt's failure to meet the threshold requirement for invoking §32(c)(2).

Based upon these findings, this Court cannot say that the bankruptcy judge abused his discretion.

Appendix B

Conclusion

The Court having found that the bankruptcy judge's findings of fact were not clearly erroneous, and that he did not commit error in concluding that the bankrupt failed to keep adequate records, and did not abuse his discretion in denying discharge, the bankrupt's petition is dismissed and the bankruptcy judge's order is affirmed.

So Ordered.

Dated: New York, New York
September 5, 1978

/s/ Lawrence W. Pierce
Lawrence W. Pierce
U.S.D.J.

APPENDIX C

UNITED STATES DISTRICT COURT

Southern District of New York

75 B. 119

In the Matter of:

Jacob P. Lefkowitz,

Bankrupt.

Order

Jacob P. Lefkowitz, appellant-bankrupt, appeals from the decision of the bankruptcy judge denying him discharge as provided by §14(c)(2) of the Bankruptcy Act, 11 U.S.C. §32.

The decision of the bankruptcy judge is hereby affirmed. Opinion to follow.

/s/ Lawrence W. Pierce
Lawrence W. Pierce
U.S.D.J.

Dated: New York, N.Y.
June 30, 1978

APPENDIX D

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

In Bankruptcy

No. 75 B 119

In the Matter

—of—

JACOB P. LEFKOWITZ,

Bankrupt.

DECISION ON OBJECTIONS TO DISCHARGE
FILED BY TRUSTEE

PRESENT:

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185 Madison Avenue
New York, New York 10016

MICHAEL BERMAN, Esq.
Attorney for Trustee
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HOWARD SCHWARTZBERG, *Bankruptcy Judge*

The trustee in bankruptcy of the above-captioned bankrupt filed a complaint objecting to his discharge in bankruptcy on three separate grounds, namely: 1. The bankrupt allegedly failed to keep books of account or records from

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which his financial condition and business transactions might be ascertained, within the meaning of §14c(2) of the Bankruptcy Act. 2. The bankrupt allegedly committed an offense punishable by imprisonment as provided under Title 18, United States Code, Section 152, as set forth in §14c(1) of the Bankruptcy Act, in that he knowingly and fraudulently made a false oath by failing to list his law library in Schedule B-2 of his schedules in bankruptcy and in testifying in this proceeding that the law library had been transferred to his son. 3. The bankrupt failed to explain satisfactorily losses in assets in excess of $2,000.00, to meet his liabilities.

The bankrupt's answer denies all three charges. At the trial, the trustee in bankruptcy was permitted to withdraw the third charge, with the result that the trial proceeded on the first two grounds only. As to the first ground, namely the bankrupt's alleged failure to keep books of account or records, the trustee stipulated that his proof would be directed to the years 1973 and 1974 exclusively.

FINDINGS OF FACT

1. On January 27, 1975, the bankrupt filed his voluntary petition in bankruptcy with this court. In accordance with §18f of the Bankruptcy Act, such filing operated as an adjudication, which in turn, acted as an application for a discharge pursuant to §14a of the Act.

2. At all times in question the bankrupt was engaged in the practice of law, specializing in criminal litigation. Apparently the bankrupt's practice was successful and his gross income was substantial. However, for the period between 1962 and 1974, the bankrupt sustained heavy gambling debts, causing him to borrow sizeable amounts of

money. He testified that at times he paid interest at the rate of 100%. He also paid interest at 50% and 25% rates. The bankrupt's schedules reveal that his unsecured obligations exceed $2,200,000. The bankrupt asserted that many of his creditors were fully paid and that their claims represent interest only.

3. Many of the people to whom the bankrupt is indebted for monies borrowed are not personally known to him. The loans were obtained through more than a half dozen middle men who acted for people who were willing to advance money at high interest rates.

4. The bankrupt testified that in his practice of law he did not have any accounts receivable. His practice was mainly in defending persons charged with crimes. They paid him in advance for his services so that billing records were not necessary. The bankrupt said that approximately twenty clients each year would be sufficient to generate a substantial income. He testified that the records reflecting his receipt of fees from clients in the years 1973 and 1974 were to be found by comparing his office diaries for these years [Exhibits 15 and 16] with all his bank deposit slips for 1973 and 1974 [Exhibits 8 and 9], all of which he produced.

5. The bankrupt's diaries contain the names of his clients, the dates when they were interviewed and statements concerning apperances to be made on their behalf. No reference is made as to any specific fees received by the bankrupt. However, the bankrupt testified that a bank deposit noted on his deposit slips for 1973 and 1974 at, or shortly after, a diary date for a named client would reflect the fee received

by him from that client. The deposit slips do not indicate the source of the money deposited. The bankrupt testified that all of his income from his law practice for the years in question was reflected on the deposit slips for those years and that by comparing the diary information with the deposit slips he could point out when he received fees from his clients and the amounts thereof. The trustee contends that these records alone are inadequate to reveal the source of the bankrupt's income; that he should not be required to enlist the assistance of the bankrupt to explain the transactions and that the records alone should be sufficient to ascertain the bankrupt's financial condition and business transactions.

6. The bankrupt had also turned over to the trustee his check books for the years in question [Exhibits 1, 2, 30, 31 and 32] his cancelled checks and all his bank statements for three years [Exhibit A]. These records indicate the payments made by the bankrupt from his checking accounts but do not carry any information as to the source of the money received by the bankrupt. He also produced copies of his income tax returns filed with Internal Revenue Service for the years 1972 [Exhibit D], 1973 [Exhibit C] and 1974 [Exhibit 10]. The 1974 income tax return reveals that the bankrupt took a deduction in the sum of $168,000. as interest on indebtedness, which the bankrupt testified represented the interest he paid on his various loans. His 1973 interest deduction was $46,511.40.

7. With respect to the bankrupt's repayment of monies borrowed, he turned over to the trustee copies of pages from a pocket memorandum book reflecting some of his short term loans and payment dates [Exhibit 3]. As to his long term loans, the bankrupt gave the trustee eleven sheets

of paper containing names of lenders, amounts of interest to be paid and the names of the middle men who had obtained the various loans for him [Exhibit 4]. The bankrupt produced seventeen sheets of paper purporting to reflect receipts from individuals for payment of interest to them, together with some principal payments [Exhibit 5]. The bankrupt also produced a bundle of his promissory notes dating back to 1970 [Exhibit 6]. These notes were returned to him by creditors after he satisfied various loans.

8. Apart from the fees that the bankrupt received from his law practice, which he testified were reflected on his bank deposit slips for 1973 and 1974 [Exhibits 8 and 9], he received borrowed funds from various sources which he used to repay outstanding loans, as revealed by the information contained in his check books, cancelled checks and lists of lenders. However, the bankrupt stated in an affidavit amending his Statement of Affairs, sworn to March 30, 1975, that from time to time he made several unrecorded cash payments to creditors set forth in his schedules, the dates and amounts of which he could not recollect.

8. The bankrupt filed his voluntary petition when his interest obligations on his loans could no longer be supported by his otherwise comfortable legal practice. Thus, for the calendar year 1974, the bankrupt's income tax return showed a gross income of $188,700, from which he deducted $48,000. for payroll taxes, rent and salaries, leaving a balance of $140,617. However, the bankrupt took a deduction for interest in the sum of $168,860., which after other business expenses of $52,067., resulted in a net loss of $80,310. [Exhibit 10]. Similarly, for the calendar year 1973, the bankrupt's gross income was $140,819. His deductions to-

talled $141,479.72, including interest of $46,511.40, resulting in a net loss of $660.72.

9. The bankrupt's deposit slips for the years 1973 and 1974 total $1,257,109.49 [Exhibit 8] and $349,492.85 [Exhibit 9], respectively. Thus, after deducting his business expenses of $79,614.73 and interest that he claimed to have paid on his indebtedness in the sum of $46,511.40, the bankrupt had an excess in deposits in 1973 amounting to $1,115,-629.77. After subtracting the bankrupt's total deductions claimed on his 1974 income tax return, amounting to $269,-010, from his deposits of $349,492.85, the bankrupt had an excess in deposits in 1974 of $80,482.85. Hence, for the two years of 1973 and 1974, the bankrupt's deposit slips reveal that he deposited $1,196,112.62 over and above his payments for interest on his indebtedness and his business expenses in those years.

10. In attempting to reconstruct the bankrupt's financial posture in 1973 and 1974, this court scrutinized the eleven pages of handwritten notes purporting to list the names of the bankrupt's long-term lenders, the dates the loans were made and the amount of interest to be paid to these lenders [Exhibit 4]. The bankrupt asserts that where a name has been crossed out this represents repayment of the loan. These pages do not indicate how many payments were made to any lender nor do they reveal the balance owed either totally or to any one lender. This court has totalled the principal amounts shown as originally owed to those lenders whose names were not crossed off, arriving at the sum of $1,699,000. However, this total is of no significance since it cannot be ascertained from these sheets how much is owed to any or all of the listed lenders at any given time or how much was paid by the bankrupt in 1973 and 1974.

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11. The bankrupt has also produced pages extracted from his pocket diary for the year 1974 reflecting his notations with respect to the names of individuals who loaned him money for short periods of time, together with the dates and interest to be paid [Exhibit 3]. The amounts noted, as best as can be determined, total approximately $250,000. However, it cannot be ascertained from this exhibit how much of this money was repaid or the total remaining unpaid balance.

12. The bankrupt asserts that most of the loans and repayments were made by cash and that interest payments were almost all made by cash at the request of the lenders. Therefore the check books and cancelled checks produced by the bankrupt are of little assistance in untangling precisely how much he repaid in 1973 and 1974, and to whom.

13. In all instances when a loan was made to him, the bankrupt contends that he gave a promissory note to the lender and that the notes were returned to him upon repayment of the principal. In reviewing the bundle of 102 returned promissory notes submitted by the bankrupt, [Exhibit 6] this court found the total to be $1,128,500.

14. Additionally, the bankrupt produced a bundle of handwritten sheets of paper containing signed receipts and notations of payment in 1974, which this court has found to total $38,275. [Exhibit 5.]

15. Upon arriving at the figure of $1,128,500 as the total face amount of the bundle of returned promissory notes [Exhibit 6] the court could not then deduct this figure from the bankrupt's total deposits in 1973 and 1974 [Exhibits 8 and 9] in an effort to ascertain whether disposition of the

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deposited sums could be explained. The very first note at the top of the bundle to which the exhibit number had been affixed bears the attached notation that this $10,000 note, dated August 25, 1970 had been replaced by another note dated September 10, 1970 "for $135,000 for one year." Thus, it cannot be ascertained how many notes in this bundle were replaced by other notes in this bundle in lieu of satisfaction of the principal face amount. Moreover, included in this bundle were one note dated August 20, 1971 for $15,000 and sixteen notes bearing dates in 1972, totalling $97,500, which cannot be presumed to have involved the disposition of funds deposited by the bankrupt in 1973 and 1974.

16. The accountant who prepared the bankrupt's income tax returns for 1973 and 1974 obtained the gross income and expense figures from the bankrupt. He was solely concerned with the bankrupt's income from his practice of law and had no interest in his borrowings, other than the figure for interest deduction, which he obtained from the bankrupt.

17. The nub of the trustee's position is that the bankrupt failed to keep records in reasonably understandable form as to the source of his receipt of funds. It stretches credulity not to expect that an able and experienced trial lawyer would not have a list of how much each client paid him during any given year. The deposit slips cannot stand as evidence of the receipt of his fees because they contain no notations as to the source of the funds deposited. Similarly, the bankrupt's income tax returns are insufficient because they are simply self-serving conclusions derived from information furnished by the bankrupt without any supportive details.

18. The bankrupt's deposit slips reveal that he deposited a total of $1,606,602.34 during the two years in question.

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The trustee and his creditors are entitled to know with a reasonable degree of accuracy how the bankrupt disposed of these funds. To conclude that most of these funds were channelled to his lenders by way of interest and principal necessitates some organized records from which the payments can be traced and the unpaid balances ascertained.

19. From the foregoing, it is evident that the disordered mass of documents produced by the bankrupt are inadequate to ascertain his financial condition and business transactions. The bankrupt has failed to sustain his burden of maintaining and presenting records in a reasonably understandable form.

20. The trustee also urges that the bankrupt's discharge should be denied because his sworn schedules are allegedly false, in that he did not list his law library as an asset.

21. The court finds that in 1972 the bankrupt's law library was not up to date because he was past due on the bills from various law book publishers. The bankrupt's son, Richard, who is a lawyer and shared space in the bankrupt's office, agreed with the bankrupt to take over the library and assume payment of all future bills. The bankrupt verbally transferred his library to his son, who had the billing transferred to his name, paid the outstanding bills and continued to assume the payments for all bills thereafter.

22. Although there is some question as to those payments made by the bankrupt's son from a joint checking account, known as "Lefkowitz & Lefkowitz", especially since the funds in this account were supplied by the bankrupt, it is clear that the son assumed responsibility for the library

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after the account was transferred to his name. Although many library payments were made by the bankrupt's son from his own account, he did make some payments from the joint account, on the theory that this was a method of obtaining repayment for amounts owed to him by the bankrupt for legal services rendered. Apart from the issue of a potentially voidable transfer for insufficient consideration, the fact remains that the bankrupt's library was transferred to his son.

23. Accordingly, this court does not find that the bankrupt's failure to list the law library in his schedules amounted to a false oath.

24. The foregoing Findings of Fact were made upon the final submission of briefs and exhibits from both parties. The trustee's brief was filed on June 8, 1976. The bankrupt's brief was filed on September 9, 1976.

DISCUSSION

This is not the case of a bankrupt whose discharge is questioned because he failed to keep *any* books or records from which his financial condition and business transactions might be ascertained as required by §14c(2) of the Bankruptcy Act. See *White* v. *Schoenfeld*, 117 F.2d 131 [2 Cir. 1941], *Nix* v. *Sternberg*, 38 F.2d 611 [8 Cir. 1930], cert. den. 282 U.S. 838; *In re Bank*, 34 F. Supp. 706 [W.D.N.Y. 1940]. Nor is this a case where a compulsive gambler is denied a discharge for failing to keep records detailing his extensive gambling transactions. See *Gaudet* v. *Cowen*, 297 F.2d 227 [5 Cir. 1961], cert. den. 370 U.S. 950; *Klein* v. *Morris Plan Industrial Bank of New York*, 132 F.2d 809 [2 Cir. 1942].

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This case involves a very experienced and competent trial lawyer whose practice over a considerable number of years in representing criminal defendants yielded him a substantial income which was allegedly consumed in the repayment of large and numerous loans which he procured to pay off previously incurred gambling losses. The trustee in bankruptcy charges that the records that the bankrupt did produce, although numerous in quantity, simply are not sufficient to account for the bankrupt's receipt of fees from his clients or for his repayments to over one hundred and fifty lenders who are listed in the bankrupt's schedules annexed to his petition and included among his unsecured creditors. The trustee has confined his proof to the two years immediately preceding the filing of the bankrupt's petition, namely 1973 and 1974.

The court is mindful of the general rule that the Bankruptcy Act was intended to permit an honest debtor to get a fresh start free from debt, and that §14 of the Act must be construed strictly against the objections and liberally in favor of the bankrupt. In re *Adlman*, [2 Cir. Sept. 14, 1976 Dkt. No. 76-5003]; *In re Kokoszka*, 479 Fed 990, 997 [2 Cir. 1973], aff'd sub nom. *Kokoszka* v. *Belford*, 417 U.S. 642; *In re Tabibian*, 289 F.2d 793, 795 [2 Cir. 1961]. However, in order to invoke the benevolent spirit of the Bankruptcy Act, §14c(2) mandates that the bankrupt must make a complete disclosure of his financial condition by producing such books and records from which the bankrupt's financial condition and business transactions might be ascertained with a reasonable degree of accuracy. *In re Underhill*, 82 F.2d 253 [2 Cir. 1936] cert. den. *Underhill* v. *Lent*, 299 U.S. 546; *International Shoe Co.* v. *Lewine*, 68 F.2d 517 [5 Cir. 1934]. The records need not state in detail all of the transactions if they sufficiently identify the trans-

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actions so that intelligent inquiry can be made concerning them. *Hedges* v. *Bushnell*, 106 F.2d 979 [10 Cir. 1941]; *International Shoe Co.* v. *Lewine*, supra.

In the *Underhill* case supra, the bankrupt sustained heavy losses from extensive stock market trading. He also withdrew large amounts from two estates in which he was a trustee. For books of account he produced certain records including his income tax returns, some cancelled checks, check books with some blank stubs and some, but not all, of his monthly brokerage statements. In reversing the granting of the bankrupt's discharge, the Court of Appeals noted that no bank deposit books were submitted; no duplicate deposit slips were produced; some items of receipts by the bankrupt were unexplained as to whether, where and how they were expended and his failure to keep stubs of cancelled checks showed such neglect as to be tantamount to an attempt to conceal transactions. The court stated the governing rule as follows: [P. 260]

> "It was never intended that a bankrupt, after failure, should be excused from his indebtedness without showing an honest effort to reflect his entire business and not a part merely. To be sure, there may be records which are not books; but it is intended that there be available written evidence made and preserved from which the present financial condition of the bankrupt, and his business transactions for a reasonable period in the past may be ascertained. Records of substantial completeness and accuracy are required so that they may be checked against the mere oral statement or explanations made by the bankrupt."

The bankrupt in the instant case was obligated to reveal his financial condition arising out of his legal practice and

extensive borrowing transactions. He produced his income tax returns for the two years in question which revealed that his gross income in those years was $188,700 and $140,819. He failed to produce any intelligible records disclosing how he arrived at these sums. Surely a self-employed lawyer would be expected to maintain some list or record detailing the amount of fees received from each of his clients during the year. Here the bankrupt testified that his practice consisted of lengthy criminal trials and that approximately twenty clients each year were sufficient to generate his fees for that year. He testified that he could scan the bundle of bank deposit slips that he produced as evidence of his receipts and identify which deposits represented fees from clients. Neither the two bundles of bank deposits for the two years in question, totalling deposits of $1,606,602.34, nor the bankrupt's monthly bank statements described the source of the funds. As was aptly stated in *In re Manasse,* 125 F.2d 647, 649 [7 Cir. 1942]:

> "Here we have the case of a lawyer who was well aware of the requirement that he keep books which would truly reflect his financial condition, and fully competent to do so."

The bankrupt's indifference to his responsibility to maintain intelligible records carried over to his pyramiding borrowings and repayments. His check book and cancelled checks from six different banks were of little value since most of the loans and repayments were made by cash. The eleven pages of handwritten notes purporting to list the bankrupt's long-term lenders and the extracts from his 1974 pocket diary containing notations as to his short-term lenders do not reflect how much was repaid nor how much was owed during any specific period. Manifestly, the bankrupt has a duty to keep his records in a reasonably understandable form. His creditors are not required to risk the concealment of assets under the guise of a chaotic set of records. *Burchett* v. *Myers,* 202 F.2d 920 [9 Cir. 1953].

The bundle of returned notes produced by the bankrupt for the two years in question would tell very little about the amount of repayments made if some of them represented the replacement of older notes with new notes, as is indicated on several of the notes. Moreover, there is no clear and complete documentation that the bankrupt paid $46,511.40 in interest in 1973 and $168,000 in interest in 1974, as claimed on the bankrupt's income tax returns for those years. Although those figures may be correct, honesty is not enough. As a condition precedent for obtaining a discharge under §14 of the Bankruptcy Act the bankrupt must either produce such records as are customarily kept by a person doing the same kind of business, or must satisfy the court why he was not duty bound to produce them. *In re Herzog,* 121 F.2d 580 [2 Cir. 1941] cert. den. 315 U.S. 807; *White* v. *Schoenfeld,* 117 F.2d 131 [2 Cir. 1941]. This the bankrupt has not done.

Conclusions

1. The court is satisfied that the bankrupt has failed to keep or preserve books of account or records, from which his financial condition and business transactions might be ascertained, as mandated by §14c(2) of the Bankruptcy Act.

2. The bankrupt has failed to show any justification for such failure.

3. The objection of the trustee in bankruptcy to the bankrupt's discharge is sustained and an order denying the discharge shall be entered by the court.

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4. The trustee has failed to prove that the bankrupt made a false oath within the meaning of §14c(1) of the Bankruptcy Act and Title 18, United States Code, §152 by failing to list his former law library in Schedule B-2 of his schedules in bankruptcy and in his testimony in this proceeding that the law library had been transferred to his son.

Dated: Yonkers, New York
September 28, 1976.

/s/ HOWARD A. SCHWARTZBERG
HOWARD A. SCHWARTZBERG
Bankruptcy Judge.

APPENDIX E

BANKRUPTCY ACT & RULES

Section 14(c)(2) (11 U.S.C. 30(c)(2), 1976) *Discharge when Granted.*

The court shall grant the discharge unless satisfied that the bankrupt has . . . (2) destroyed, mutilated, falsified, concealed, or failed to keep or preserve books of account or records, from which his financial condition and business transactions might be ascertained, unless the court deems such acts or failure to have been justified under all the circumstances of the case; . . .

Provided, That if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this subdivision c, would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt.

Rule 407

BURDEN OF PROOF IN OBJECTING TO DISCHARGE

At the trial on a complaint objecting to a discharge, the plaintiff has the burden of proving the facts essential to his objection.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 78-1781

In the Matter

—of—

JACOB P. LEFKOWITZ,

Bankrupt-Petitioner.

SUPPLEMENTAL PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 78-1781

In the Matter

—of—

JACOB P. LEFKOWITZ,

Bankrupt-Petitioner.

SUPPLEMENTAL PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

ADDITIONAL REASON FOR GRANTING THE WRIT

1. The opinion of the Court of Appeals (Appellant's Appendix 1a-3a) sought to be reviewed is in conflict with a very recent decision of the Third Circuit Court of Appeals, *In Re Decker*, 20 C.B.C. 173 (CA-3, 1979, 78-2007), (Supplemental Appendix, 1sa-8sa) holding that Bankruptcy Rule 407 places the burden of persuasion upon the trustee seeking to deny a discharge, under Section 14c(2) of the Bankruptcy Act, to prove the inadequacy of the bankrupt's books and records.

Decker involved a real estate developer with assets in excess of $62 million and liabilities of $56 million, who

filed a petition for a real property arrangement under Chapter XII of the Bankruptcy Act, 11 U.S.C. 801-926, (1976), who was subsequently adjudicated a bankrupt. The trustee objected to Decker's discharge, *inter alia*, on the grounds that Decker failed to produce accurate and complete records of his affairs. The Bankruptcy Court denied his discharge and the District Court affirmed.

The Third Circuit reversed the District Court and remanded it for further proceedings consistent with its opinion. The Court of Appeals concluded that it was evident from the cases cited therein, that the Bankruptcy Judge has misapplied the standard of proof required by Bankruptcy Rule 407 and had erroneously applied the standard of proof as set forth in the proviso to Section 14c of the Bankruptcy Act, which the Court of Appeals determined to be now defunct. Under Section 14c, as mentioned previously, the burden of ultimate persuasion shifted to the bankrupt once the objector had made out a *prima facie* case. But under Rule 407, as the Circuit Court correctly held, the burden of persuasion was at all times on the trustee.

The Court elaborated by stating that a trial judge is not compelled to accept a plaintiff's testimony even if uncontradicted. (Id. at 179) Even in the absence of an explanation by a bankrupt, such is not, in and of itself, enough to compel a Bankruptcy Judge to accept a trustee's allegations. The trustee carries the burden of proving all the elements of his allegations.

The case at bar presents a situation similar to that of the *Decker* case. Although the Bankruptcy Judge and the affirming District and Circuit Courts paid lip service to Rule 407, it is obvious from their respective opinions that they were applying the standard of proof contained in the

proviso to Section 14c of the Bankruptcy Act, which standard of proof has been superseded by Rule 407, in effect since October 1, 1973.

The Bankruptcy Judge's decision is replete with examples of his misapplication of the current law. A reading of the Bankruptcy Judge's findings of fact clearly shows that the Bankruptcy Judge, contrary to the letter of the law, placed the burden of proof and explanation upon the bankrupt.

In Paragraph 6, (15a), the Bankruptcy Judge, while admitting that the bankrupt turned over to the trustee all of his checkbooks, cancelled checks and bank statements, found these records inadequate to show the source of the monies received by the bankrupt. But then, in Paragraph 8, (16a), the Judge contradicts himself by stating that "he (bankrupt) received borrowed funds from various sources which he used to repay outstanding loans, as revealed by the information contained in his checkbooks, cancelled checks and list of lenders". The bankrupt, in his testimony, stated that his diaries reflected the source of monies, whether fees or loans, and that by correlating the diaries with deposit slips, he could determine who paid him and what the purpose of the payment was, and also, when such payment was deposited. The veracity of the bankrupt's unrebutted testimony was never in issue or questioned.

Again in Paragraph 17, (19a), the Bankruptcy Judge states that deposit slips could not stand as evidence of the receipt of fees because they lacked notations as to the source of the monies deposited. This is in direct contradiction to the testimony given by the bankrupt wherein he explained that because he had only fifteen to twenty clients per year, he did not require an intricate bookkeeping sys-

tem and was able to ascertain fees given by correlating the dates of the deposit slips with notations in his diaries.

Finally, the Bankruptcy Judge held that because the records produced were disordered, they were inadequate to ascertain the financial condition and business transactions of the bankrupt, Paragraph 19 (20a). However, the Bankruptcy Judge failed to note that the documents were in such a state only because the trustee deliberately presented them in that manner. They had been delivered in an original correlated condition but presented in disarray by the trustee. Despite this fact, the bankrupt was able to explain each and every transaction which took place. The trustee failed to bring to light any specific instances in which the bankrupt was unable to adequately explain all business transactions.

The tenor throughout the Bankruptcy Judge's summation of law also reflects a belief on his part that the bankrupt carried the burden of proof as to the adequacy of his records. The Bankruptcy Judge, in his opinion, created a 'condition precedent' for obtaining a discharge under Section 14 of the Bankruptcy Act wherein such condition precedent does not exist. (25a) Section 14c(2) states that a Court *shall* grant a discharge unless satisfied that the bankrupt failed to keep or preserve records from which his financial condition might be ascertained. Rule 407 requires the trustee, in order to block a discharge under Section 14c(2), to prove the records are inadequate. Thus, unless the trustee proves the records are inadequate, the discharge must be granted as a matter of course. *Liebke* v. *Thomas*, *supra*. The condition precedent, if any, is upon the trustee to prove his objection.

The District Court's opinion affirming the Bankruptcy Court is also quite obviously tainted with the view that

the bankrupt must disprove the charge of inadequate records. The Court held that the Bankruptcy Judge was within his authority in finding that "documents which can be made intelligible only through his 'interested' testimony —which the judge may or may not credit—has failed to adequately establish the financial condition as required by the Act". (8a) The bankrupt's "interested" testimony consisted of presenting his checkbooks, diaries, deposit slips, cancelled checks, pocket memoranda, a vast amount of promissory notes and letters from lenders and his unrebutted and uncontradicted oral testimony. At no time during the trial was the bankrupt at a loss to explain any and all of his business transactions, as was reflected by the records presented by the trustee. Additionally, the bankrupt's testimony was buttressed by that of his accountant, whose testimony was also uncontradicted.

The Court of Appeals further compounded the lower courts' mistakes by affirming the decisions below and holding that "Rule 407 in no way relieves the (bankrupt) of his burden of producing adequate records". (3a) The Court of Appeals has thereby approved the legal concept of placing the burden of proof on the shoulders of the bankrupt, rather than the objecting trustee, which is at conflict with the decision of the Third Circuit.

Certiorari should be granted, so as to resolve the apparent conflict between the Court of Appeals for the Second and Third Circuits, and thereby promulgate a clear standard of proof required in objections to discharge under this Section of the Bankruptcy Act and the new Bankruptcy Code.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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Supplemental Appendix

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Sotelo, 436 U.S. 268, 274, 56 L.Ed.2d 275, 281, 98 S.Ct. 1795, 1801, 11 U.S.C.A. § 35(a)(1)(e),[3] that a § 6672 liability, whether or not levied within three years preceding bankruptcy, is not dischargeable in bankruptcy. Appellant's argument to the contrary bears no merit.

Alternatively, appellant argues for the first time on appeal, that he was not a "person required to collect, truthfully account for, and pay over any tax" within the meaning of § 6672. Since we find no indication in the record that appellant raised this contention or supported it by controverting affidavits before the Bankruptcy Judge or the District Court, we hold that, on the facts before the Court, summary judgment was properly granted.

Affirmed.

In the Matter of MARTIN M. DECKER and KATHLEEN H. DECKER, Bankrupts

No. 78-2007

(3d Circuit, C.C.A., March 26, 1979. Before: Hunter and Weis, Circuit Judges and Stapleton, District Judge*)

The bankrupt was denied a discharge under Section 14c(2) of the Act on the ground that he had failed to keep or preserve books of account or records from which his financial condition and material business transactions might be ascertained. The district court affirmed.

On appeal, the Court of Appeals reversed, holding that the burden of proof as to the adequacy of the records had been improperly imposed on the bankrupt rather than on the trustee. Though Section 14c(2) had placed the burden of proof on the bankrupt, this provision was superseded by Bankruptcy Rule 407.

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[3] 11 U.S.C.A. § 35(a)(1)(e) states that

"[a] discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as (1) are taxes which became legally due and owing by the bankrupt to the United States or to any State or any subdivision thereof within three years preceding bankruptcy: *Provided, however*, That a discharge in bankruptcy shall not release a bankrupt from any taxes (e) which the bankrupt has collected or withheld from others as required by the laws of the United States or any State or political subdivision thereof, but has not paid over; * * *."

* Of the United States District Court for the District of Delaware, sitting by designation.

[1] Rule 407. Denial of Discharge Because of Inadequate Records; Burden of Proof.

Rule 407 supercedes Section 14c(2) with respect to the burden of proof allocation, and thus the burden of persuasion rests upon the trustee in seeking to deny a discharge, to prove the inadequacy of the bankrupt's records. (Collier on Bankruptcy, 14th ed., **12:**407.3[1])

HUNTER, Circuit Judge: 1. Martin M. Decker, the bankrupt, appeals from the district court's judgment denying him a discharge in bankruptcy under section 14c(2) of the Bankruptcy Act, 11 U.S.C. § 32(c)(2) (1976). The district court, in affirming the bankruptcy judge, determined that Decker failed to keep or preserve books of account records from which his financial condition and material business transactions might be ascertained. Because we believe that the bankruptcy judge improperly imposed on the bankrupt, rather than the Trustee, the burden of proof with regard to the adequacy of the records, we reverse.

I

2. Decker was a real estate developer in the Philadelphia area, owning and managing office buildings, luxury high-rise apartment buildings, and other income producing property. On February 12, 1971 three creditors filed an involuntary petition in bankruptcy against him. Shortly thereafter, Decker filed a voluntary petition for a real property arrangement under Chapter XII of the Bankruptcy Act, 11 U.S.C. §§ 801-926 (1976). Price Waterhouse & Co., which had been retained by Decker to assist in the preparation of a financial statement, reported that as of the date of the filings, Decker had assets of $62 million and liabilities of $56 million. However, Decker did not file a plan for the satisfaction of his debts, and on July 10, 1972 he was adjudged bankrupt.

3. On September 6, 1974 the Trustee in Bankruptcy, Morris Gerber, filed a complaint under section 14c of the Bankruptcy Act objecting to Decker's discharge in bankruptcy. After a hearing, the bankruptcy judge found no merit in the Trustee's objection and granted the discharge. The Trustee appealed and the district court remanded "for the purpose of [the Trustee's] presenting all relevant testimony to support [his] position." Before hearing the case on remand, the bankruptcy judge who had handled the case since its filing retired, and a replacement was appointed.

4. The newly appointed bankruptcy judge considered three objections by the Trustee to Decker's discharge. Two of the grounds, essentially alleging intentional concealment of property, were dismissed. However, on April 4, 1977 the bankruptcy judge denied the discharge solely on the ba-

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sis of the Trustee's third objection, that Decker had failed to keep books of account or records from which his financial condition and material business transactions might be ascertained.

5. The bankruptcy judge noted two major record keeping errors which he used to justify a denial of the discharge. First, the court listed ten specific journal entries which he stated "disclose[d] a pattern of careless, haphazard bookkeeping uniquely ill-suited to an enterprise of the size and complexity of the Decker organization." Generally, the entries illustrated Decker's failure to record major transactions until several months after they had occurred. The judge noted, however, that documentation existed to support each questionable entry. Second, and of particular importance in his opinion, the judge cited testimony by the Trustee's accountant which indicated that Decker's cash ledger account reflected at least $200,000 and perhaps as much as $370,000 for which an origin could not be ascertained. The bankruptcy judge noted that "[a]ll the other myriad inadequacies of the Bankrupt's bookkeeping system pale by comparison."

6. In reviewing the evidence, the bankruptcy judge placed the burden on the Bankrupt to disprove the Trustee's allegations of inadequate records. He stated that "[i]f the evidence is in a state of 'substantial equilibrium,' the discharge should be denied." Further, he explained that he ruled "against [the Bankrupt] only where no explanation was available." Thus, the bankruptcy judge held that Decker had not demonstrated that he had fulfilled the "high degree of duty to present to his creditors, represented by the Trustee, a substantially accurate and complete record of his affairs" and denied the discharge.

7. On appeal the district court regarded the bankruptcy court's determination that Decker's records were inadequate within the meaning of section 14c(2) as a finding of fact. Reviewing under the clearly erroneous standard, the court affirmed the denial of the discharge. Decker appeals.

II

[1] 8. Section 14a of the Bankruptcy Act, 11 U.S.C. § 32(a), provides that "the adjudication of any person, except a corporation, shall operate as an application for a discharge." A bankrupt is entitled to a discharge unless the court is satisfied that the bankrupt has committed one of the acts listed in section 14c. Here, the Trustee filed a complaint under section 14c(2).[1] To prevail, the Trustee must show that the Bankrupt failed

[1] Section 14c of the Bankruptcy Act, 11 U.S.C. § 32(c) (1976), provides in part:

"The court shall grant the discharge unless satisfied that the bankrupt has . . . (2) destroyed, mutilated, falsified, concealed, or failed to keep or preserve books of account or records, from which

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to keep or preserve books of account or records and that the failure makes it impossible to ascertain the financial condition and material business transactions of the bankrupt. *In re Leichter*, 197 F.2d 955, 958 (3d Cir. 1952), *cert. denied*, 344 U.S. 914 (1953); 1A Collier on Bankruptcy ¶ 14.33, at 1370 (14th ed. 1973). While "the statute does not exact as a condition precedent to the granting of a discharge the keeping of an impeccable system of bookkeeping which would meet the approval of a skilled accountant or records so complete that they would satisfy an expert in business," the records must "sufficiently identify the transactions that intelligent inquiry can be made of them." *Johnson v. Bockman*, 282 F.2d 544, 546 (10th Cir. 1960). The test is whether "there [is] available written evidence made and preserved from which the present financial condition of the bankrupt, and his business transactions for a reasonable period in the past may be ascertained." *In re Underhill*, 82 F.2d 258, 260 (2d Cir.), *cert. denied*, 299 U.S. 546 (1936).

9. While the trial court has wide discretion in determining whether the books or records are sufficient within the meaning of the statute, *Goff v. The Russell Co.*, 495 F.2d 199, 202 (5th Cir. 1974), this court has stressed the "well-settled principles that the right to a discharge is statutory, and that Section 14 of the Bankruptcy Act must be construed strictly as against the objector and liberally in favor of the bankrupt." *In re Leichter*, 197 F.2d 955, 957 (3d Cir. 1952), *cert. denied*, 344 U.S. 914 (1953). *Accord, In re Pioch*, 235 F.2d 903, 905 (3d Cir. 1956).

10. Decker's major contention on appeal is that the bankruptcy judge improperly allocated the burden of persuasion. He points out that the judge imposed the burden on the bankrupt in accordance with the proviso to section 14c of the Bankruptcy Act. However, he contends that the proviso has been superseded by Bankruptcy Rule 407, which would place the burden, as in most civil actions, on the objector to prove that the bankrupt is not entitled to a discharge.

11. In explaining the framework in which he reviewed the evidence, the bankruptcy judge stated:

> "Once the trustee has demonstrated reasonable grounds for believing that the Bankrupt has committed the offense, the Bankrupt

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his financial condition and business transactions might be ascertained, unless the court deems such acts or failure to have been justified under all the circumstances of the case; . . . *Provided*, That if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this subdivision, would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt."

5 so

has the burden of proof of persuading the court that the allegations in the specifications are untrue. If the evidence is in a state of "substantial equilibrium", the discharge should be denied because the Bankrupt has failed to carry his burden. *Gunzburg v. Johannesen*, 300 F.2d 40 (5th Circuit, 1952).

Thus, the judge applied the burden of proof as outlined in the proviso to section 14c:

> "*Provided*, That if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this subdivision, would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt."[2]

The proviso has been interpreted as shifting the ultimate burden of persuasion, not just the burden of going forward with the evidence, to the bankrupt once the objector makes out a prima facie case that the bankrupt is not entitled to a discharge. *In re Finn*, 119 F.2d 656, 657 (3d Cir. 1941). *Accord, In re Melnick*, 360 F.2d 918, 919-20 (2d Cir. 1966); *Feldenstein v. Radio Distributing Co.*, 323 F.2d 892, 893 (6th Cir. 1963); *Johnson v. Bockman*, 282 F.2d 544, 545 (10th Cir. 1960).

12. The bankruptcy judge's citation to *Gunzburg v. Johannesen*, 300 F.2d 40 (5th Cir. 1962), leaves little doubt that he believed that as a matter of law the burden of ultimate persuasion shifted to the bankrupt once the objector made out a prima facie case. In *Gunzburg*, the court stated: "This is more than the burden of going forward with the evidence. For '. . . the bankrupt now has the risk of ultimately persuading the Court that the allegations in the specifications are untrue.' " *Id.* at 41.

13. However, Bankruptcy Rule 407 became effective on October 1, 1973. It provides:

> "At the trial on a complaint objecting to a discharge, the plaintiff has the burden of proving the facts essential to his objection."

The Advisory Committee Note to Rule 407 specifically states: "The rule supersedes the proviso at the end of § 14c of the Act." The cases which have considered the effect of Rule 407 on the proviso have held that the bankruptcy judge must allocate the burden of persuasion in accordance with Rule 407. *See, e.g., Matter of Martin*, 554 F.2d 55, 58 n.1 (2d Cir. 1977); *Matter of Tucker*, 399 F. Supp. 660, 662 (S.D. Fla. 1975). The Trustee filed his complaint objecting to Decker's discharge in September,

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[2] *See* note 1 *supra*.

1974. Therefore, if Rule 407 is valid, the bankruptcy judge erred as a matter of law in applying the proviso to section 14c.

14. At argument, and for the first time in the case, the Trustee contended that Rule 407 was an impermissible exercise of the United States Supreme Court's rule-making power. Under 28 U.S.C. § 2075 (1976), the Supreme Court has the power to prescribe rules for practice and procedure under the Bankruptcy Act which do not "abridge, enlarge, or modify any substantive right."[3] The Trustee contends that Rule 407, by placing the burden of ultimate persuasion on the objector rather than the bankrupt, modifies a substantive right. There is a strong presumption, however, that the Supreme Court did not abridge or modify any substantive rights by the adoption of the Bankruptcy Rules. *Matter of Mobile Steel Co.*, 563 F.2d 692, 699 (5th Cir. 1977); *In re Wall*, 403 F. Supp. 357, 360 (E.D. Ark. 1975). Other than the naked assertion at argument, the Trustee has made no attempt to overcome that presumption. We hold that Rule 407 is a valid exercise of the Supreme Court's rule-making power and should have been applied.[4]

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[3] The Bankruptcy Rules enabling statute, 28 U.S.C. § (1976), provides:

> "The Supreme Court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure under the Bankruptcy Act.
>
> "Such rules shall not abridge, enlarge, or modify any substantive right.
>
> "...
>
> "All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect."

[4] We are aware that in the context of Erie R.R. v. Tompkins, 304 U.S. 64 (1938), "burden of proof" has been held to be substantive rather than procedural. Palmer v. Hoffman, 318 U.S. 109, 117 (1943); Cities Service Oil Co. v. Dunlap, 308 U.S. 208, 212 (1939); Fireman's Fund Ins. Co. v. Videfreeze Corp., 540 F.2d 1171, 1174 (3d Cir. 1976), *cert. denied*, 429 U.S. 1053 (1977).

However, as the Supreme Court noted in Hanna v. Plumer, 380 U.S. 460, 471 (1965), "[t]he line between 'substance' and 'procedure' shifts as the legal context changes." There, the Court examined whether Federal Rule of Civil Procedure 4(d)(1) prescribes the proper method of service in a diversity suit when the state statute requires in-hand service. The issue was whether the Federal Rule modified "substantive" rights, thereby exceeding the Supreme Court's rule-making powers under 28 U.S.C. § 2072 (1976). The Rules Enabling Act is virtually identical to the Bankruptcy Rules enabling statute, 28 U.S.C. § 2075. *See* note 3 *supra*. The Court rejected the outcome determinative test as the means of distinguishing between "substantive" and "procedural" under the Rules Enabling Act. Instead, it interpreted "procedural" broadly to include "matters which relate to the administration of legal proceedings." 380 U.S. at 472, *quoting* Lumbermen's Mutual Casualty Co. v. Wright, 322 F.2d 759, 764 (5th Cir. 1963).

Professor John Hart Ely in his widely cited article on the substantive/procedural distinction under the Rules Enabling Act has proposed a more elaborate definition:

> "[A] procedural rule . . . is one designed to make the process of litigation a fair and efficient mechanism for the resolution of disputes. Thus, one way of doing things may be chosen over another because it is thought to be more likely to

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15. Without questioning the validity of Rule 407, at least one authority has interpreted the rule as having only limited application to section 14c(2). 12 Collier on Bankruptcy ¶ 407.3[1] (14th ed. 1975). This interpretation arises because section 14c(2) provides that the bankrupt may demonstrate an excuse for his failure to keep or preserve adequate records. Thus, the first part of section 14c(2) states the general rule: the bankrupt will not be granted a discharge if the objector establishes that the records are inadequate to disclose the bankrupt's financial condition and material business transactions. But the second part of that subsection allows the court to grant the discharge even if the records are inadequate if "the court deems such acts or failure to have been justified under all the circumstances of the case." *Collier* argues against applying Rule 407 to the "justification" provision because the information necessary to establish an excuse for inadequate or non-existent records is generally in the bankrupt's possession.

16. We need not decide whether Rule 407 requires the objector to bear the burden of persuasion on the issue of "justification." Decker has made no attempt to invoke the "justification" provision. Rather, he contends that his books and records are sufficient to entitle him to a discharge under the Act.

17. Finally, our determination that the bankruptcy judge improperly allocated the burden of persuasion is not altered by his statement at the conclusion of his opinion that he "accepted every explanation offered by the Bankrupt, ruling against him only where no explanation was available." With the burden of persuasion on the Trustee, the absence of an explanation by Decker is not enough in itself to compel the bankruptcy judge to accept the Trustee's allegations. A trial judge "is not compelled to accept a plaintiff's testimony even if uncontradicted. The plaintiff has

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get at the truth, or better calculated to give the parties a fair opportunity to present their sides of the story, or because . . . it is a means of promoting the efficiency of the process."

Ely, *The Irrepressible Myth of Erie*, 87 Harv. L. Rev. 693, 724-25 (1974) (footnotes omitted). *See* McCollum Aviation, Inc. v. Cim Associates, Inc., 438 F. Supp. 245, 247-48 (S.D. Fla. 1977) (adopting the Ely formulation).

We feel that the distinction between substance and procedure in the Rules Enabling Act is applicable to the Bankruptcy Rules enabling statute. The allocation of the "burden of proof" in this context is appropriately viewed as a rule of procedure "thought to be more likely to get at the truth," *id.* at 725. In fact if we were to recognize any distinction between the tests under the two statutes, we would be apt to grant the Supreme Court even greater leeway under the Bankruptcy Rules statute. Any constitutional considerations which may be inherent in a federal court's decision whether to apply the rules of a state or the Federal Rules of Civil Procedure, *see* Hanna v. Plumer, 380 U.S. at 474-78 (Harlan, J., concurring), are certainly inapplicable in the bankruptcy context, where only federal law and policy are at issue.

the burden of proof and the trial judge may find that the testimony does not carry that burden." *Santana v. United States*, 572 F.2d 331, 335 (1st Cir. 1977).

III

18. The bankruptcy judge, as affirmed by the district court, placed the ultimate burden of persuasion on the bankrupt. We hold that Bankruptcy Rule 407 supersedes the proviso to section 14c and should have been applied to impose the burden of persuasion on the Trustee. It is not for this court in the first instance to apply the appropriate burden of proof to the evidence.[5]

19. Therefore, the judgment of the district court will be *Reversed*, and the case remanded for proceedings consistent with this opinion.

In re WILLIAM MAIDMAN, Bankrupt

No. 75-1249-BK-CA-H

(S.D. Florida, March 30, 1979,
C. Clyde Atkins, Chief District Judge)

Maidman had obtained a discharge in bankruptcy. The trustee moved, in bankruptcy court, to dismiss a subsequent Chapter XI petition and to consummate a sale of assets held by the trustee. The bankruptcy court denied the trustee's motions and ordered the bankrupt to file an affidavit regarding the bidding for assets.

On appeal, the district court affirmed, holding that a Chapter XI petition may be filed at any time a case is pending, before or after adjudication. The court further held that if the affidavit filed by the bankrupt pursuant to the order of the bankruptcy court was insufficient, the sale to the trustee should be consummated.

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[5] The disposition of this case has been unnecessarily complicated by the apparent refusal of the successor bankruptcy judge to rule on whether the hearings held on remand from the district court constituted a trial de novo or merely an additional hearing to supplement the record. The transcript of the hearings reflects numerous requests by the attorneys for both sides to get these lines defined. They were not.

Because of the legal error committed by the bankruptcy judge on the allocation of the burden of proof, we have not been compelled to resolve this issue. However, to eliminate the continuation of this problem, the proceedings on remand should be de novo.

In The

Supreme Court of the United States

October Term, 1978

No. 78-1781

In the Matter

of

JACOB P. LEFKOWITZ,

Bankrupt-Petitioner.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

REASONS FOR DENYING THE WRIT

This brief is submitted on behalf of Jerome Schulman as Trustee in Bankruptcy of Jacob P. Lefkowitz, Bankrupt, in opposition to the petition of Jacob P. Lefkowitz for a writ of certiorari to the United States Court of Appeals for the Second Circuit.

The petitioner has based his application for a writ of certiorari upon the following questions (the response to these questions follow each of the questions):

QUESTIONS PRESENTED AND RESPONSE THERETO

Question 1.

Does the Bankruptcy Act and Rules require the bankrupt to first prove the adequacy of his financial records where admittedly no records were destroyed or concealed and the bankrupt produced *all primary or original records*, such as, checkbooks, deposit slips, bank statements, cancelled checks and the like, *before* a party objecting to his discharge need demonstrate the facts essential to the objection?

Response:

The petitioner contends that since he produced a large quantity of records, consisting of checkbooks, deposit slips, bank statements and cancelled checks that that fulfilled his obligation to maintain books of account or records from which his financial condition and business transactions might be ascertained, as required by Section 14c(2) of the Bankruptcy Act. The fact of the matter is that the petitioner maintained no books of account and the records that he produced failed to comply with the requirements of said Section as shall hereinafter appear.

The checkbooks produced by the petitioner indicated bank accounts in approximately six different banks. They failed to indicate in any manner whatsoever, the deposits made in the account, the source thereof, or the nature and purpose of the withdrawals of moneys except as indicated by the payee on the checks.

The deposit slips maintained by the petitioner indicated deposits in his several bank accounts which for the years 1973 and 1974 totalled $1,257,109.49. An examination of the deposit slips indicated that the majority of the deposits were made in

cash and failed to reflect the source of the deposits. In 1973 only six deposit slips out of several hundred indicated the source of the cash deposit. In 1974 only one deposit slip indicated the source of the cash deposit.

The petitioner maintained that he kept a record of receipts received from his clients in his diary or in his deposit slips. The diaries produced by petitioner failed to indicate any list of clients except entries therein referring to a pending matter. The deposit slips failed to indicate the names of the clients except in the few instances referred to.

The petitioner's federal income tax returns for the years 1973 and 1974 disclosed that petitioner, an attorney-at-law, had a gross income of $188,700 in 1973 and $140,819 in 1974. The income tax returns failed to indicate the source of the deposits or the disposition of the moneys received by him except in general terms.

It is obvious that the records produced by the petitioner failed substantially to indicate his financial condition and business transactions.

Question 2a:

Whether the court below erred, by misconstruing and misapplying Section 14(c) of the Bankruptcy Act, 11 U.S.C. Section 32(c) (1976), and Congress' intent by imposing an unduly harsh standard as to the adequacy of the bankrupt's books and records merely because of his profession, unjustly denying the bankrupt his discharge?

Response:

Petitioner urges that Rule 407 of the Bankruptcy Rules places the burden of proving the facts essential to an objection on the objector. This in no way relieves the petitioner of his

burden of producing adequate records. *See* Advisory Committee Note to Rule 407; *In the Matter of Martin*, 554 F. 2d 55, 58 (2d Cir. 1977), *cert. dismissed*, 434 U.S. 801 (1978).

In the case of *In re Underhill*, 82 F. 2d 258, 260 (2d Cir.), *cert. denied*, 299 U.S. 546 (1936), the Court held:

> "Records of, substantial completeness and accuracy are required so that they may be checked against the mere oral statement of explanations made by the bankrupt. [Citation omitted.]"

There is nothing in the record which indicates that the bankruptcy judge placed any burden on the petitioner forbidden by Rule 407 of the Bankruptcy Rules. The records produced by the petitioner did not meet the statutory mandate which required him to produce records from which his financial condition and business transactions might be ascertained.

Under Rule 752 of the Rules of Bankruptcy Procedure the findings of fact of a bankruptcy court should not be set aside unless clearly erroneous and due regard should be given to the opportunity of the trial court to judge the credibility of the witnesses. Rule 810 of the Rules of Civil Procedure contains a similar provision.

In the case of *Simon v. Agar*, 299 F. 2d 853, the Court of Appeals for the Second Circuit, in interpreting General Order 47, the predecessor of these rules, said the following:

> "It is too well settled to require the citation of authorities that where an appeal brings up for review concurrent findings of fact by the referee and the district court, they can be set aside only if 'clearly erroneous'. See Bankruptcy General Order 47, 11 U.S.C.A. following section 53; Rule 52(a) F. R. Civ. P., 28 U.S.C.A. Particularly is this true where, as in this case, the findings involve questions of credibility of witnesses who testified before the referee. See Morris Plan Industrial Bank v. Henderson, 2 Cir., 131 F. 2d 975, 977; Margolis v. Nazareth Fair Grounds & Farmers Market, Inc., 2 Cir., 249 F. 2d 221, 223; Smith v. United States, 5 Cir., 287 F. 2d 299, 301. Appellant has not carried his burden of convincing us that both essential findings are clearly erroneous."

The findings of the bankruptcy court have been sustained by the district court and the court of appeals.

Question 2b:

Considering the rehabilitative intent of the Bankruptcy Act, did the court below err in failing to remand, to permit the bankrupt to organize, *i.e.*, write up in ledgers his primary or original records so that these secondary ledgers or records would then reflect his financial condition and business transactions?

Response:

Petitioner is requesting the Court to permit him to write up books of account from his primary or original records. The testimony was clear at the hearing that the primary records produced by petitioner were insufficient to indicate the petitioner's financial condition and business transactions and his recollection of these transactions were not adequate under the law to permit him to write up books of account without corroborative written records.

Petitioner has failed to set forth any grounds upon which a petition for a writ of certiorari should be granted.

CONCLUSION

Wherefore it is respectfully submitted that the application by petitioner for a writ of certiorari to the United States Court of Appeals for the Second Circuit be denied.

Respectfully submitted,

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Jerome Schulman